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ABSTRACT

This paper recommends that the federal government take steps to reassert the sense of partnership and common purpose that undergirds college finance in the United States by enacting an old idea that never had become a reality. The original authorizing legislation for the Pell grant program envisioned direct institutional grants to colleges that would accompany Pell grants and help colleges absorb the costs of such grants. These "cost of education" allowances were never funded, but, in modified form, they might meet the needs of the present day. For every Pell grant recipient enrolled, a college would receive a given amount, perhaps $2,500. This flat "capitation" grant has the virtue of simplicity. It rewards colleges for enrolling Pell grant students without giving them any incentive to raise prices, as would an increase in the Pell grant. Such a program would declare in a clear way that Congress regards institutions as partners in promoting college opportunity. It would reinforce the commitment of colleges to the education of disadvantaged students. (SLD)

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Getting the Most Out of Federal Student Aid Spending – Encouraging Colleges and Universities to Promote the Common Good

Michael S. McPherson & Morton Owen Schapiro

Research Report #6

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The College Board
National Dialogue On Student Financial Aid

Research Report 6

PATHWAYS to COLLEGE NETWORK

JANUARY 2003

GETTING THE MOST OUT OF FEDERAL STUDENT AID SPENDING—ENCOURAGING COLLEGES AND UNIVERSITIES TO PROMOTE THE COMMON GOOD

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The American system of college finance can only work if the federal government works as a partner with individual colleges and universities in helping families pay for college.[1] It's hard to imagine how this nation could sustain its remarkably high levels of college access and opportunity, together with the high level of decentralization and diversity among colleges, without such a partnership. The distinctive form of partnership that has shaped American college finance since the 1960s has been built around the idea of measuring and meeting families' need for financial assistance in paying for college. Although with significant differences among their roles, all the partners have operated on a roughly agreed set of principles: that more aid should go to students with greater need, that aid should be available to students regardless of where they choose to attend, and that access to a worthwhile college experience should be available to all without regard to ability to pay.

For the most part, policy disputes in college finance for many years took the form of "family squabbles" about exactly how to work out the details of the partnership. Were the formulas for dispensing federal aid to students at public and private institutions fair in their treatment of the sectors? How far into the (ill-defined) "middle class" should federal, state, and institution-based aid extend? How did state policies of low public tuition for all fit into a largely needs-oriented (and hence means-tested) conception of support for college finance? How should the needs of adult students be thought about in a scheme that was basically constructed around the image of a fresh 18-year-old high school graduate going off to college? How should private scholarships, awarded say by corporations or foundations, fit into a needs-oriented system?

In recent years, the terms of debate have shifted and the sense of partnership has become somewhat frayed. At the federal level, tax credits have become an increasingly important device for helping families manage college expenses, and these are not easily calibrated to need (nor does Congress seem much interested in such calibration). Individual colleges and universities have come increasingly to see financial aid awards as strategic tools to get the students they want while maximizing their net tuition revenues; as a result, merit-sensitive award mechanisms have grown in importance. And states have felt both pulls: expanding their own use of tax and savings incentives, and building larger merit components into their award systems.[2]

Not surprisingly, these developments have made it harder for governmental and institutional leaders to think of one another as participants in a common—and indeed a noble—enterprise. Congress has spent a good deal of time worrying that colleges might "capture" some portion of the stream of tax credit dollars that they are aiming at the wallets of middle- and upper middle-income families. In a similar vein, the Department of Education, in developing its Gear Up program to encourage high school students to attend college, attempted to prevent colleges from reallocating their own aid funds away from students who received awards under Gear Up. That is, the presumption was that colleges would divert the released resources

1. The federal government is a relatively modest player in the big picture of higher education finance, but one with great potential leverage. For a detailed analysis of changes over time in revenue sources, see Michael S. McPherson and Morton Owen Schapiro, *The Student Aid Game: Meeting Need and Rewarding Talent in American Higher Education*, Princeton University Press, 1998.

2. At the institutional level, published figures on non-need-based aid greatly understate the actual role of merit in financial aid awards (see Michael S. McPherson and Morton Owen Schapiro, "The Blurring Line Between Merit and Need in Financial Aid," *Change*, Vol. 34, No. 2, March/April 2002, pp. 38–46). In terms of state financial aid funding, between 1995-96 and 1998-99, the real increase in state spending on need-based aid was 13.2 percent, while the real increase in non-need-based aid was 58.6 percent. In 1999–2000, state spending on need-based aid rose by 8.5 percent while non-need based aid rose by 22 percent. In 1994-95, merit-based grant expenditures comprised 15 percent of all state student aid funding, a figure that rose to 22 percent by 1999–2000. (All state figures are computed from data in the *Chronicle of Higher Education*.)

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toward unworthy purposes, rather than leveraging these resources to enable more disadvantaged students to get to college. Some members of Congress seem to see colleges not so much as the vehicles through which educational opportunities are extended, but rather as obstacles that interfere with the relations between Congress and their middle-class constituents.

For their part, colleges, and especially their Washington associations, view with growing suspicion any federal initiatives in areas like data collection or accountability standards, fearing that they will turn into oppressive efforts at federal regulation and micromanagement. While relations between state governments and colleges vary greatly across the nation, it is probably fair to say that by and large there has been movement from debate around how to achieve agreed policy goals toward a bare-knuckled struggle over resources.

Yet, notwithstanding the mutual suspicion, the bottom-line reality is that colleges, the federal government, and state governments all need one another to meet college goals. We believe that it is time for the federal government to take a bold step to reassert the sense of partnership and common purpose that undergirds college finance in the United States. The vehicle we propose for accomplishing this is an old idea that never quite became a reality.

The legislative history makes clear that, in the early days of what is now the Pell grant program, Congress conceived federal student aid grants to students from low-income families as a means of helping colleges do something the colleges themselves very much wanted to accomplish—that is, to help poor kids and to increase the economic diversity of their campuses.[3] Indeed, recognizing that educating disadvantaged students would add to college costs, the original authorizing legislation for these grants envisioned direct institutional grants to colleges that would accompany Pell grants and help institutions absorb these costs. Although these "cost of education" allowances were never funded, their presence in the authorizing legislation speaks loudly of the sense of partnership of those days.

We propose resurrecting these "cost of education" allowances, in modified form, to meet needs of the present day. To get the idea on the table, imagine first a simple version of these allowances: For every Pell grant recipient a school enrolled, the college where she enrolled would receive a $2,500 grant. This policy would have three great things in its favor.

First, it would make the college's financial calculation of enrolling Pell grant students rather than more affluent students more favorable. Most college leaders do value this goal, but the economics of pursuing it, for all but the most affluent campuses, are daunting. At most private colleges, students who qualify for a Pell grant will also require a substantial grant of institutional aid in order to afford attendance. A private college that is hungry for enrollment (as most are) has to calculate that a grant of (say) $10,000 to a needy Pell recipient could instead allow two low-need "merit" recipients to enroll with awards of $5,000 each. A $2,500 grant to the college doesn't overcome this difference, but it does make the calculation significantly less discouraging. The effect would probably be even greater at public universities and community colleges, where a $2,500 institutional grant is a much larger fraction of the tuition charge.

Second, such a program would declare in a clear way that Congress recognizes that institutions are indeed partners in promoting college opportunity. There are extra costs for colleges if they want to do a good job in educating students who have grown up in disadvantaged economic and educational backgrounds, as most Pell recipients do. Cost of education allowances would encourage colleges to promote enrollment of and success for these students, and would imply public acknowledgement of the worth of such efforts.

Third, and importantly, cost of education allowances would accomplish these things without providing colleges any incentive to raise prices. If the federal government simply raised the average Pell grant award by $2,500, low-priced colleges (principally community colleges or other low-priced publics) would have an incentive to raise their prices to qualify their students for larger awards (by raising their "need" levels). This program has no such adverse incentive effects.

This $2,500 flat "capitation" grant has the considerable virtue of simplicity, but various refinements are possible. One obvious objection to the proposal is that it would provide substantial payments to colleges for efforts they are already undertaking. A response to that concern would be to provide cost of education allowances only for increases in the number of Pell enrollees relative to recent experience. Another possible concern is that the proposal makes no distinction in the rewards to colleges for enrolling more disadvantaged versus less disadvantaged Pell recipients. To meet this challenge, one could proportion the size of the cost of education allowance to the size of the Pell grant, or alternatively

3. See Lawrence E. Gladieux and Thomas R. Wolanin, *Congress and the Colleges: The National Politics of Higher Education*, Lexington, Mass.: Heath, 1976.

provide the allowances only in response to Pell awards that were above a certain level (say $1,500). Finally, some might want to introduce an explicit performance component into cost of education allowances. One might therefore provide the allowances only in recognition of students who successfully completed the year's study or (like the Bundy program in New York) upon successful attainment of a degree.

Clearly by far the biggest challenge in getting this proposal considered is the very idea that Congress would authorize sending checks directly to colleges to support their efforts. This, we think, is an argument worth having. To put it bluntly, we think Congress should get over the idea that a dollar going directly to a college or university is a dollar wasted. Both the Pell program and federally supported loan programs emphasize putting the money into students' hands and letting them choose. This "individualistic" and market-oriented dimension of federal support is important and worthwhile. Indeed, the proposal we have made would also move money to schools as students "voted with their feet" about where to attend. But our proposal recognizes that, in addition to bolstering individuals' capacity to finance education, we need also to reinforce colleges' commitment to the education of disadvantaged students and to provide support to help them do it well.

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